

OFFICE OF THE
ARIZONA
STATE
TREASURER



HON. DOUG DUCEY
TREASURER

INVESTMENT
PHILOSOPHY

SAFETY
before
LIQUIDITY
before
YIELD



Treasurer Doug Ducey
Arizona State Capitol
1700 W. Washington St.
Phoenix, AZ 85007

(602) 542-7800
toll free (877) 365-8310

info@aztreasury.gov
www.AZTreasurer.gov



Inside the Vault

The Arizona State Treasurer's Quarterly Update

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Q1 2013

Arizona's Pension Systems: Final Report

The health and sustainability of our pension systems is of critical importance to everyone in Arizona. These benefits are funded from tax dollars and from the employees themselves. The State of Arizona sponsors four retirement systems that currently cover more than 581,000 employees, retirees, or former employees who have yet to retire.

Much of the discussion surrounding any pension system revolves around complicated financial formulas.

There is an equally important human element that must always be in the forefront; these pensions are for those who teach our children, police our streets, put out the fires, respond to medical emergencies, and keep the basic functions of government running.

As of June 30, 2012, Arizona's pension plans have unfunded liabilities ranging from \$18.4 billion to \$39.6 billion depending on what discount rate is used, and using the market valuation of the plans' assets. In addition to a growing unfunded liability, the number of retired members in each of the four retirement systems is growing faster than the number of new workers entering.

Arizona's retirement plans are professionally and competently managed. We are fortunate that our pensions are in far better shape than many other states. That said, there are issues that require attention. Several reform options were explored by the Study Committee for policy makers to consider so Arizona can continue to strengthen and enhance those plans in order to protect the benefits to current retirees and employees that have earned them, as well taxpayers now and in the future.

The final report, as well as all the meeting minutes, presentations and research materials can be accessed by visiting <http://www.aztreasury.gov/defined-contribution-retirement-study-committee/>.

Pension Plan Deficits on the Rise



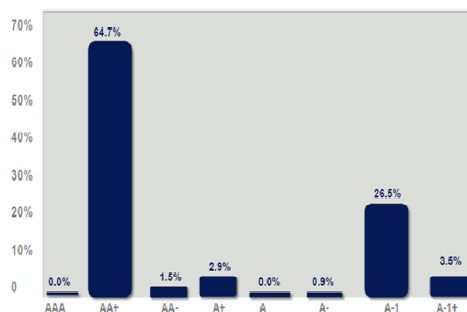
LGIP Pool 5: Short-term fund

AT A GLANCE

- \$1.36 Billion in assets with Net Asset Value at \$1.000 as of 12/31/2012.
- Diversified investments weighted to highly rated Commercial Paper first, Repurchase Agreements second and Agencies/Treasuries third.
- Continues to maintain the highest rating of AAAF/SI+.
- Weighted Average Maturity is 23 days.
- We expect a choppy quarter as the market digests money moving from banks into funds, plus ongoing financial policy debates.

Safety

Continues to receive highest rating from Standard & Poor's: AAA/SI+

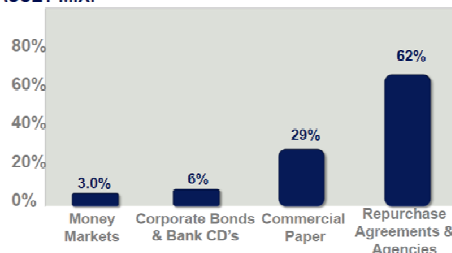


Liquidity

Weighted Average Maturity: 23 days on 12/31/2012

DURATION: 100% from 0-1 yrs

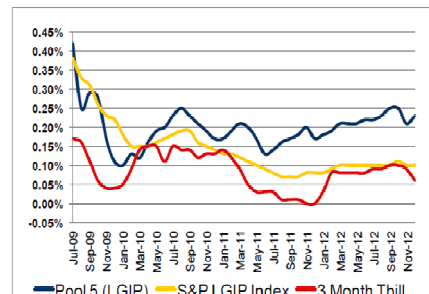
ASSET MIX:



Yield

.23% FYTD

.10% FYTD (S&P LGIP Index)

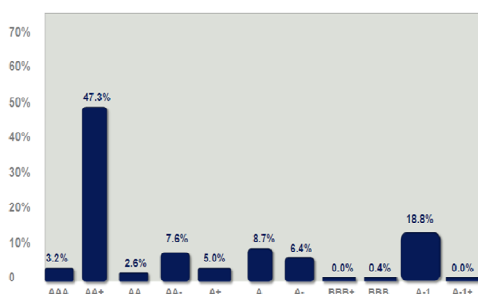


**Pool 5 YTD
Net Yield
has beaten its
benchmark by
13 basis points**

LGIP Pool 500: Medium-term fund

Safety

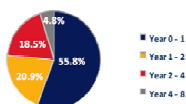
AA Weighted Average Rating



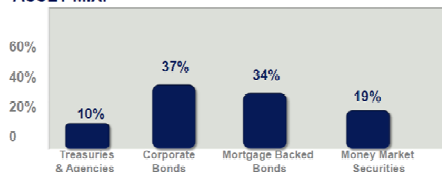
Liquidity

Effective Duration: 1.21 years on 12/31/2012

DURATION:



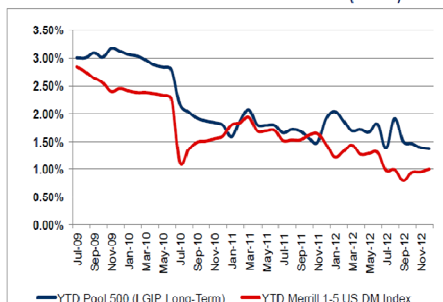
ASSET MIX:



Yield

1.50% FYTD

0.94% FYTD (Index)



**Pool 500 YTD
has beaten its
benchmark by
56 basis points**

AT A GLANCE

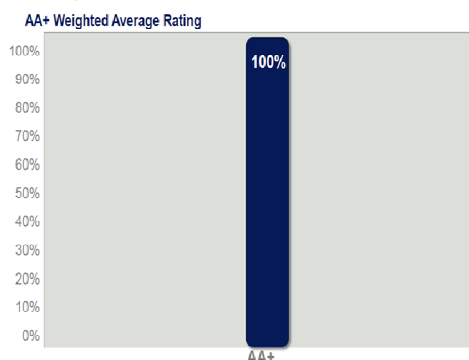
- \$275 Million in assets with Floating Net Asset Value at \$1.0434 as of 12/31/2012.
- Diversified fund containing Treasuries, Agencies, Corporate Bonds and Mortgages.
- The effective duration is 1.21 years.
- Keeping the fund short with 76.8% of the investments maturing under two years.
- Maximum exposure to any credit at 2.5%.
- Weighted Average Rating of all the securities is AA.

Pool 7 LGIP-GOV: Short-term fund

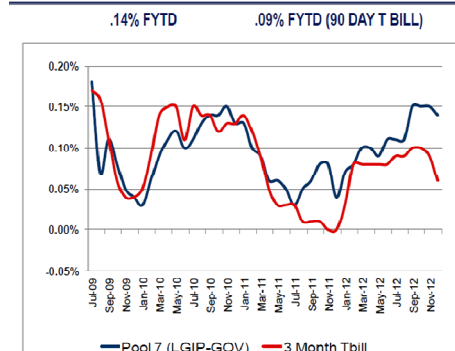
AT A GLANCE

- \$1.36 Billion Assets with Net Asset Value at \$1.00 as of 12/31/2012.
- Invested in highly liquid, low-risk securities that are backed by the full faith and credit of the U.S. Government.
- Overall rating is AA+, which reflects the S&P downgrade of U.S. debt.
- Weighted Average Maturity is 45 days.
- We expect rates to decline for the quarter as the federal fiscal issues have caused supply and demand imbalances in the overnight repo market.

Safety



Yield

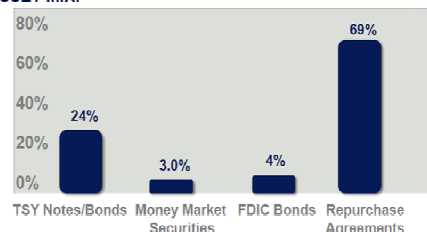


Liquidity

Weighted Average Maturity: 45 days on 12/31/2012

DURATION: 100% from 0-1 yrs

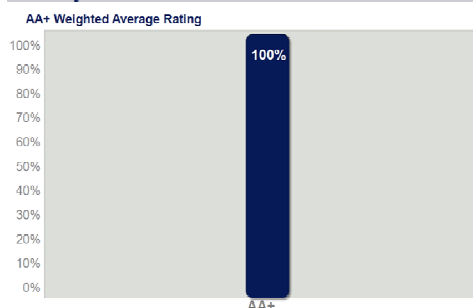
ASSET MIX:



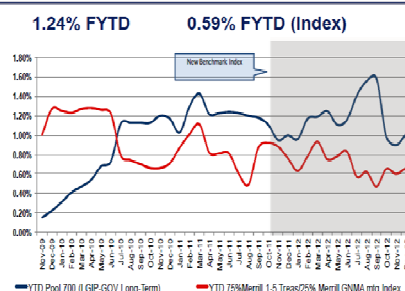
**Pool 7 YTD
Net Yield
has beaten its
benchmark by
5 basis points**

Pool 700 LGIP-GOV: Medium-term fund

Safety



Yield



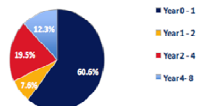
AT A GLANCE

- \$222.9 Million in assets with Floating Net Asset Value at \$1.0169 as of 12/31/2012.
- All securities are backed by the full faith and credit of U.S. Government including Treasuries, FDIC paper and GNMA Mortgages.
- The effective duration is 1.44 years.
- Keeping the fund short with 86% of the investments maturing in under two years.
- Weighted Average Rating of all the securities is AA+.

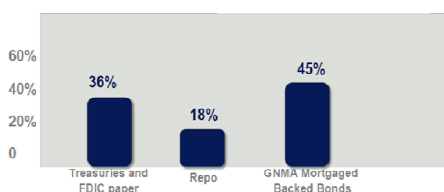
Liquidity

Effective Duration: 1.44 years on 12/31/2012

DURATION:



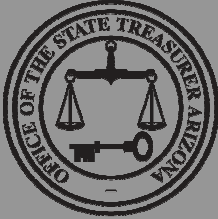
ASSET MIX:



**Pool 700 YTD
has beaten its
benchmark by
65 basis points**

OFFICE OF THE

ARIZONA STATE TREASURER



INVESTMENT PERSONNEL

Mark Swenson
Deputy Treasurer
(602) 542-7877

Carlton Woodruff
Deputy Treasurer
Operations
(602) 542-7875

Patricia Humbert
Sr. Portfolio Manager
(602) 542-7841

Tim White
Sr. Portfolio Manager
(602) 542-7836

Chris Petkiewicz
Portfolio Manager
(602) 542-7839

Dale Stomberg
LGIP Investment
Accounting
(602) 542-7833

Lorraine Jones
Revenue Distributions
(602) 542-7818



View AZ's Daily Cash Balance at www.AZCheckbook.com

Arizona's State Debt = \$8.7 Billion

The Joint Legislative Budget Committee (JLBC) delivered their annual report of Arizona's State Debt and the status of other financial obligations to the Appropriations Committees in both the Senate and House. Although the Legislature has gone to great lengths to deliver balanced budgets and begin to save money in the "Rainy Day Fund" the past two years, there are several areas on the state's balance sheet that still need to be addressed.



Highlights of the presentation include:

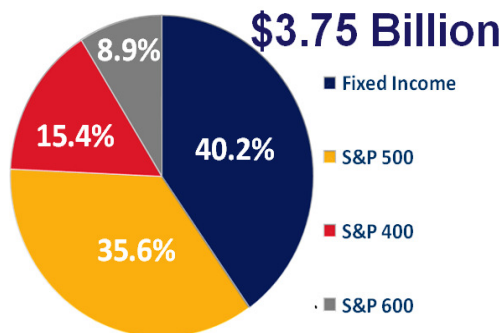
- Total Outstanding State Debt = **\$8.71 billion**;
- Debt Obligations Have Increased Significantly From **\$4.89 billion** in FY07;
- The State Defers **\$1.2 billion** of Payments Annually;
- General Fund Share of the Outstanding Debt Balance = **\$3.6 billion**;
- FY12 General Fund Debt Service Cost = **\$302 million** (7th largest budget item);
- Debt Service Costs will increase to **\$373 million** in FY14.

The entire report, which includes debt retirement options and a listing of all lease-purchase/bonding issuances from FY03, can be accessed online at

<http://www.aztreasury.gov/wp-content/uploads/2012/02/JLBC-State-Debt-PPT.pdf>.

Land Endowment Asset Allocation

(as of December 31, 2012)



AZ's Checking Account

**FY 2013 Q2 Average
Monthly Cash Balance:**

+65% YOY

**October = \$1.205 Billion
November = \$1.306 Billion
December = \$1.463 Billion**

AZ's Savings Account (as of December 31, 2012)

\$452,099,810

Monthly Interest Earned:

**October = \$374,670
November = \$321,742
December = \$317,588**

**FY 2013 Q2 Earnings
\$58,562,508**

